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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-1161

GAF CORPORATION,
Conditional Cross-Petitioner,

v.

PAUL MILSTEIN, SEYMOUR MILSTEIN, GLORIA MILSTEIN FLANZER and MORRIS MILSTEIN,
Respondents.

CONDITIONAL CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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CONDITIONAL CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The conditional cross-petitioner GAF Corporation ("GAF") respectfully prays that a writ of certiorari issue to review that portion of the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this proceeding on December 13, 1971 encompassed within the question presented below, the writ to issue only in the event this Court should grant the petition for a writ of certiorari in No. 71-1144, filed this Term (the "principal petition").

OPINIONS BELOW

The opinion of the Court of Appeals for the Second Circuit, not yet reported, is annexed as Appendix A to the

principal petition and the opinion of the United States District Court for the Southern District of New York, reported at 324 F. Supp. 1062 (S.D.N.Y. 1971), is annexed to such petition as Appendix B.[1]

JURISDICTION

The judgment of the Court of Appeals for the Second Circuit was entered on December 13, 1971, and this conditional cross-petition for certiorari will be filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

QUESTION PRESENTED

Does an issuer claiming violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder have standing to seek injunctive relief against purchasers of more than $2.5 million of its securities who, in furtherance of a secret agreement to attempt to acquire control of the issuer, filed Schedules 13D pursuant to Section 13(d) of the Securities Exchange Act of 1934 (the "1934 Act") and Rule 13d-2 promulgated thereunder with the issuer, the Securities and Exchange Commission (the "Commission"), and the exchanges on which the issuer's shares are traded falsely disclaiming any intention to acquire additional securities of the issuer and otherwise making untrue statements of material fact and omitting to state material facts which would have made such Schedules 13D not misleading?

1. References to the opinion of the Court of Appeals below are to pages of Appendix A to the principal petition and appear, for example, as (PP App. A 7a). References to the District Court opinion are to pages of Appendix B to the principal petition and appear, for example, as (PP App. B 7b).

STATUTES AND REGULATIONS INVOLVED

The underlying action is for injunctive relief based on violations of Sections 10(b) and 13(d) of the 1934 Act, 48 Stat. 891 and 82 Stat. 454, 15 U.S.C. §§ 78j(b) and 78m(d), and of Rules 10b-5 and 13d promulgated thereunder by the Commission, 17 C.F.R. §§ 240.10b-5 and 240.13d. Portions of Section 13(d) are set forth as Appendix C to the principal petition and Section 10(b) and Rule 10b-5 are set forth in full below:

Section 10(b):

> "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> "(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Rule 10b-5:

> "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,
>
> "(a) To employ any device, scheme, or artifice to defraud,
>
> "(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

> "(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security."

STATEMENT OF THE CASE

A. Basis for Federal Jurisdiction.

Federal jurisdiction in the District Court is based on Section 27 of the 1934 Act, 63 Stat. 107, 15 U.S.C. § 78aa, which states in relevant part:

> "The district courts of the United States . . . shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and all suits in equity and actions at law brought to enforce any liability or duty created by this chapter or the rules and regulations thereunder."

B. The Proceedings Below.

GAF, the plaintiff below, is a publicly owned corporation organized under the laws of the State of Delaware [6a] whose shares are traded on the New York and other stock exchanges and owned by more than 125,000 persons.[2] The respondents, defendants below, are four stockholders, Paul Milstein, his brother Seymour Milstein, his sister Gloria Milstein Flanzer and his father Morris Milstein (the "Milsteins") [6a].

On December 16, 1970 GAF filed its complaint in this action in the District Court for the Southern District of New York charging that the Milsteins violated Section 13(d) of the 1934 Act (1) by failing to make a timely Schedule 13D filing after secretly forming a group whose mem-

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2. References, as for example [6a], are to pages in the Joint Appendix filed in the Court of Appeals for the Second Circuit.

bers owned more than 10% of GAF's preferred stock and whose purpose was to acquire control of GAF and (2) by later filing Schedules 13D which were untimely, false, misleading, and contained serious and substantial omissions of material facts [7a-13a]. The complaint also charged that the Milsteins violated Section 10(b) of the 1934 Act (1) by concealing their takeover group and its plans by means of untimely, false, and misleading 13D filings, (2) by depressing the price of GAF securities, and (3) by concurrently purchasing $2.5 million of GAF common stock [13a-15a]. The complaint sought solely injunctive relief preventing the Milsteins from acquiring any additional GAF securities, soliciting any proxies to vote GAF securities, voting any GAF securities acquired pursuant to their takeover scheme, and otherwise acting in furtherance of that scheme [15a-16a].

On January 19, 1971 the Milsteins moved to dismiss the complaint for failure to state a claim or, in the alternative, for summary judgment. On March 22, 1971 District Judge Milton Pollack dismissed the complaint on the grounds that GAF failed to state a claim for relief under Section 13(d) and that GAF lacked standing to seek injunctive relief for violations of Section 10(b) and Rule 10b-5. GAF appealed and on December 13, 1971 the Court of Appeals for the Second Circuit reversed the District Court's dismissal of GAF's 13(d) claims and affirmed the District Court's holding that GAF lacked standing to assert that the Milsteins violated Section 10(b) and Rule 10b-5.

We believe the decision of the Court of Appeals with respect to the application of Section 13(d) is eminently sound. However, the Milsteins have applied to this Court for a writ of certiorari to review the 13(d) determination. We believe that the writ should not issue and will elaborate our reasons in response to the petitioner's application. However, should this Court grant the Milsteins' application, GAF requests

that the entire decision below be reviewed and that this conditional cross-petition be granted. If, as we believe to be appropriate, the Milsteins' application is denied, GAF does not seek any further review and will pursue its remedies in the District Court in accordance with the decision of the Court of Appeals.

C. The Facts.

Since May, 1967 the Milsteins have beneficially owned not less than 10.25% of GAF's preferred stock which they acquired when The Ruberoid Company ("Ruberoid"), in which they had substantial holdings, was merged into GAF [20a-21a, 23a]. Thereafter the Milsteins determined to act together as a group to attempt to acquire control of GAF and engaged in a variety of activities in furtherance of their takeover plan [7a-15a]. During 1968, 1969 and 1970 the Milsteins in furtherance of their takeover plan sought senior management and board positions at GAF for Seymour Milstein, withdrew huge amounts of business normally placed with GAF by companies whose operations they controlled (causing GAF to lose approximately three-quarters of a million dollars in profits), sought access to information concerning GAF not lawfully available to them, sought to enlist the support of third parties in their effort to seize control of GAF, obtained confidential information and documents concerning GAF's internal affairs from present and former employees of GAF, unfairly disparaged the management of GAF, depressed the market price of GAF stock to facilitate the acquisition of additional shares, and commenced a purported derivative action, *Milstein* v. *Werner, et al.*, 70 Civ. 2178 MP (S.D.N.Y.), and a companion action in the Supreme Court of the State of New York, New York County, Index No. 19158/70 to further disparage GAF's management and depress the price of GAF stock [8a-9a].

Although the Milsteins' takeover group was formed after the enactment of the Williams bill (which became Section 13(d) of the 1934 Act), they made no attempt to comply with the Act until September 24, 1970 when they filed the first of their so-called Schedules 13D. In the meantime, between April 13 and June 9, 1970, respondents Paul and Seymour Milstein had secretly purchased 61,100 and 64,000 shares of GAF common stock, respectively, from unsuspecting GAF shareholders who had no notice whatever of their takeover group and its plans [164a, 170a].

The September 24 Schedule 13D made the following false, evasive, and misleading statements concealing the Milsteins' true intentions:

> "The members of the Milstein family have no present intention as to whether or not any additional securities of GAF may be acquired by them in the future and, accordingly, can have no present intention as to whether such purchase, if made, would be made with their personal funds or with funds or other consideration borrowed or otherwise obtained for the purpose of acquiring such securities."
>
> • • • • •
>
> "Depending on the course of corporate affairs of GAF, including this litigation [referring to *Milstein* v. *Werner, supra*], the [Milsteins] at some future time may determine to attempt to acquire control of GAF, whether through a tender offer, the solicitation of proxies, or otherwise."

and

> "[The Milsteins] find it impossible at this time to state more specifically whether they may attempt to acquire control in the future or, in the event they might acquire control in the future, what their plans would be." [20a, 21a-22a]

The Milsteins thereafter filed with GAF, the Commission, and various exchanges on which GAF's shares are traded, a second Schedule 13D dated November 10, 1970 and a third dated January 27, 1971. In the November 10 filing the above quoted statements were reiterated verbatim [28a, 30a] and in the January 27 filing the first such statement respecting the absence of any intention on their part to acquire additional GAF securities was stated again verbatim [142a].

Although each of these public filings disclaimed any intention to acquire additional GAF securities, the first and third filings were quickly followed by massive purchases of such securities [164a, 170a, Amdmt. 1 to Schedule 13D dated 2/23/71, at 3, 5] and the second Schedule 13D was certified by the Milsteins on the very day that both Paul and Seymour Milstein purchased additional GAF stock [164a, 170a]. Less than one month after the first statement was filed, *before* any correction or amendment was filed, and while the false Schedule 13D was in the public domain, Paul and Seymour Milstein continued their secret purchases of GAF securities by each purchasing 41,650 shares of GAF common stock at a cost of more than $840,000 in identical quantities through the same broker at identical prices on the same four days, October 21, 27 and 29 and November 10, 1970 [164a, 170a]. Less than two weeks after the third filing and *before* any correction or amendment was filed, Paul Milstein made the following purchases of GAF common stock: on February 8, 1971 he purchased 100 shares; on February 12, 9,800 shares; on February 16, 1,400 shares; on February 17, 16,000 shares; and on February 19, 1,000 shares. These February purchases came to light when the Milsteins filed Amendment No. 1 to Schedule 13D, dated February 23, 1971.

Further, notwithstanding the above-quoted disclaimers of intention to seek control of GAF contained in the Sched-

ules 13D dated September 24, 1970 and November 10, 1970, the Milsteins continued their secret takeover efforts until January 26, 1971 when Seymour Milstein served GAF with a demand for the inspection of GAF's list of stockholders, which demand finally admitted his "intention . . . to solicit proxies from stockholders . . . in order to elect a new Board of Directors . . . at the next meeting of stockholders. . . ." The same admission was made by Paul Milstein on January 28, 1971 [131a, 137a]. Concurrently with the demand for inspection, the Milsteins filed their third Schedule 13D under date of January 27, 1971 and Schedules 14B which set forth their plans to wage a proxy contest at GAF's annual meeting in April [138a, 143a, 162a-173a].

GAF's complaint and the corroborating evidence presented to the District Court demonstrated that the Schedules 13D filed by the Milsteins under dates of September 24, 1970, November 10, 1970 and January 27, 1971 were false and misleading in that they asserted that the Milsteins had no intention to acquire additional GAF securities, omitted material statements of the names and activities of others with whom the Milsteins were working and the sources and amounts of funds or other financial arrangements used and to be used by the Milsteins in acquiring GAF securities, and the September 24 and November 10 filings were false and misleading (as well as untimely) in that they failed to admit that the Milsteins had long before decided to try to acquire control of GAF [10a-12a]. Moreover, it is an undisputed fact of record that Paul and Seymour Milstein purchased 69,850 and 41,650 shares of GAF's common stock [164a, 170a, Amdmt. 1 to Schedule 13D dated 2/23/71], respectively, from shareholders who, in the absence of any correction or amendment, were entitled to rely upon the Milsteins' public statements disclaiming any intention to acquire any additional securities of GAF and any intention to attempt to acquire control of GAF.

REASONS FOR GRANTING THE WRIT TO REVIEW THE RULE 10b-5 QUESTION IF THE COURT DETERMINES TO REVIEW THE SECTION 13(d) QUESTION.

1. This Court should not resolve questions of interpretation of one section of the 1934 Act without deciding the applicability of other sections triggered by the same circumstances.

If this Court determines to review the judgment below as to Section 13(d), it should review the entire case. Apart from the issue of standing, the facts alleged in this proceeding trigger both Sections 13(d) and 10(b), and one section should not be interpreted without consideration of the other. "[T]he interdependence of the various sections of the securities laws is certainly a factor in any interpretation of the language Congress has chosen. . . ." *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 466 (1969).

This Court has long recognized as a canon of statutory construction that the interpretation and applicability of individual sections must be considered in the context of the whole Act:

> "We believe it fundamental that a section of a statute should not be read in isolation from the context of the whole Act, and that in fulfilling our responsibility in interpreting legislation, we must not be guided by a single sentence or member of a sentence, but [should] look to the provisions of the whole law, and to its objects and policy." *Richards* v. *United States*, 369 U.S. 1, 11 (1962) (footnotes omitted) (quoting from *Mastro Plastics Corp.* v. *Labor Board*, 350 U.S. 270, 285 (1956), *reh. denied*, 351 U.S. 980 (1956) and *United States* v. *Boisdoré's Heirs*, 8 How. 113, 122 (1850)).

In accord are *SEC* v. *National Securities, Inc., supra; Labor Board* v. *Lion Oil Co.*, 352 U.S. 282, 288 (1957);

SEC v. *Joiner Corp.*, 320 U.S. 344, 350 (1943); *Panama Refining Co.* v. *Ryan*, 293 U.S. 388, 439 (1935); *Cherokee Intermarriage Cases*, 203 U.S. 76, 89 (1906).

Meaningful decision as to the interpretation of one section of the 1934 Act arising in the context of a struggle for corporate control cannot be made in the absence of determining the role played by other complementary provisions of that Act. Standing under other sections of the 1934 Act should not preclude standing under Rule 10b-5 particularly where this Court has held that the fact that the conduct complained of is actionable under another section of the 1934 Act does not preclude the application of Section 10b and Rule 10b-5. *SEC* v. *National Securities, Inc.*, *supra* at 468-69. Accordingly, GAF respectfully urges that this Court review the 10b-5 question presented by the same facts as the 13(d) question, if it decides that the 13(d) question be reviewed at all.

2. Unlike the Section 13(d) issue, there is a substantial conflict among the Courts of Appeals on the Rule 10b-5 question.

Contrary to what the Milsteins would have this Court believe, no Court of Appeals has interpreted Section 13(d) in a manner that would require a contrary result in the case at bar. As GAF will demonstrate in its brief in opposition to the principal petition, the interpretation of Section 13(d) adopted by the Court of Appeals for the Second Circuit is entirely consistent with the interpretation of Section 13(d) adopted by the Court of Appeals for the Seventh Circuit in *Bath Industries, Inc.* v. *Blot*, 427 F.2d 97 (7th Cir. 1970), insofar as the present case is concerned.

However, the 10b-5 question presented by this conditional cross-petition has generated substantial conflict among the Courts of Appeals. In upholding an action for injunctive relief under Rule 10b-5 where the plaintiff was neither a

purchaser nor a seller, the Court of Appeals for the Third Circuit in *Kahan* v. *Rosenstiel*, 424 F.2d 161, 173 (3d Cir. 1970), *cert. denied sub nom., Glen Alden Corp.* v. *Kahan*, 398 U.S. 950 (1970), pointed out that:

> "The present case represents the first time this Circuit has addressed itself to the question whether Section 10(b) may be enforced by a private party who is neither a purchaser nor seller. *The Circuits which have decided the issue are divided.* The Seventh and Eighth Circuits require that plaintiffs be purchasers or sellers even where injunctive relief is sought. Greater Iowa Corporation v. McLendon, 378 F.2d 783 (8th Cir. 1967) (following Birnbaum); Jachimiec v. Schenley Industries, Inc., No. 15024 (7th Cir. 1965) cert. denied, 382 U.S. 841, 86 S.Ct. 46, 15 L.Ed.2d 82 (1965). The Second Circuit has construed the statute more broadly at least where an injunction is sought. The Sixth Circuit has also indicated that in a suit for injunctive relief the requirements may be liberalized. In Britt v. Cyril Bath Co., 417 F.2d 433, 436 (6th Cir. 1969), that court stated that in a suit under § 10(b), the necessary causal connection between the fraud alleged and the resultant purchase or sale of a security might be relaxed." 424 F.2d at 173 (emphasis supplied).

In the case at bar, the Court of Appeals for the Second Circuit noted that it had "steadfastly refused to extend the reach of [Rule] 10b-5 to give standing to an issuer" following "the rule of *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461 (2d Cir. 1952), *cert. denied*, 343 U.S. 956 (1952) [that]

only a purchaser or seller of a security can maintain an action under [Section 10(b)]." (PP App. A 21a).[3]

Here the issuer sought to enjoin continuing fraudulent purchases of its securities by stockholders who engaged in various activities to depress the price of such securities, publicly and falsely disclaimed any intention to acquire additional securities of the issuer, and continued to purchase large blocks of its securities from stockholders entitled to rely on the veracity and completeness of those filings. The issuer's standing was disposed of on a motion to dismiss the complaint for failure to state a claim. Accordingly, the Court, on this conditional cross-petition, is presented with a pure question of law, the ideal vehicle to develop and present its views, provide sorely needed guidance in an important but troublesome area of the law, and, at the same time, resolve a substantial conflict among the Courts of Appeals.

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3. The District Courts are in even greater conflict on the question of the issuer's standing to seek injunctive relief for violations of Rule 10b-5. Decisions upholding such standing include *Butler Aviation Int'l, Inc.* v. *Comprehensive Designers, Inc.*, 307 F. Supp. 910 (S.D.N.Y. 1969), *aff'd on other grounds*, 425 F.2d 842 (2d Cir. 1970); *Moore* v. *Greatamerica Corp.*, 274 F. Supp. 490 (N.D. Ohio 1967); *Dodge Mfg. Corp.* v. *Emerson Elec. Co.*, [1966-1967 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 91,692 (N.D. Ind. 1967); and *Franklin Realty* v. *United Nat'l Corp.*, 70 Civ. 3366 (E.D. Pa. February 18, 1971). District court decisions denying standing include *Studebaker Corp.* v. *Allied Products Corp.*, 256 F. Supp. 173, 179-80 (W.D. Mich. 1966); *Pacific Ins. Co. of N.Y.* v. *Blot*, 267 F. Supp. 956 (S.D.N.Y. 1967); *Allied Artists Pictures Corp.* v. *D. Kaltman & Co. Inc.*, 283 F. Supp. 763, 765 (S.D.N.Y. 1967); *General Time Corp.* v. *American Investors Fund, Inc.*, 283 F. Supp. 400 (S.D.N.Y. 1968), *aff'd on other grounds sub nom., General Time Corp.* v. *Talley Indus., Inc.*, 403 F.2d 159 (2d Cir. 1968), *cert. denied*, 393 U.S. 1026 (1969); *Bound Brook Water Co.* v. *Jaffe*, 284 F. Supp. 702, 708 (D.N.J. 1968), *amended complaint dismissed*, [1967-1969 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 92,243 at 97,141 (D.N.J. 1968); *Hambros Bank, Ltd.* v. *Meserole*, 287 F. Supp. 69, 72 (S.D.N.Y. 1968); *Duplan Corp.* v. *Iroquois Indus., Inc.*, [1967-1969 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 92,318 at 97,493 (W.D.N.Y. 1968).

3. Unlike the Section 13(d) issue which is limited to control situations, the Rule 10b-5 issue is more generally applicable, affecting all types of fraudulent transactions involving the issuer's securities.

The Section 13(d) question presented to the Court of Appeals, namely, whether a filing is required when individuals collectively owning beneficially more than 10% (now 5%) of a class of securities agree to act together, is confined to the relatively few situations where corporate control is actually or potentially affected. However, the question of whether an issuer has standing under Section 10(b) and Rule 10b-5 to enjoin fraudulent purchases and sales of its own securities is not limited to control situations but encompasses numerous types of fraudulent transactions. In *Superintendent of Insurance* v. *Bankers Life and Casualty Co.*, 404 U.S. 6 (1971), this Court recently emphasized that "Section 10(b) outlaws the use 'in connection with the purchase and sale' of any security of 'any manipulative or deceptive device or contrivance' . . . by 'any person,'" whether conducted in the organized markets or face-to-face, pointing out that "Section 10(b) must be read flexibly, not technically and restrictively." *Bankers Life* presented this Court with its first occasion to consider a private right of action under Section 10(b) and Rule 10b-5 and the Court (n. 10) declined to decide whether an issuer had standing under these provisions to complain of fraudulent transactions involving its securities. That question persists, however, as a substantial issue of great importance to the investing public the 1934 Act is designed to serve.

4. Unlike the interlocutory nature of the order involving the Section 13(d) claim, the Court of Appeals judgment on the Rule 10b-5 issue may well be final unless reviewed by this Court.

The Court of Appeals reversal of the dismissal of the Section 13(d) claim would, absent review by this Court, result in that claim being remanded to the District Court for further proceedings. As the Court of Appeals recognized, "we emphasize that we are not yet called upon to determine whether the Milsteins have in fact violated section 13(d) or, if they have, what relief would be appropriate" (PP App. A 23a). However, the judgment of the Court of Appeals affirming the dismissal of GAF's Rule 10b-5 claim may well be a final judgment unless now reviewed by this Court.

This Court has repeatly stated that it will not normally review nonfinal judgments. *Cobbledick* v. *United States*, 309 U.S. 323, 324-25 (1940); *Hamilton-Brown Shoe Co.* v. *Wolf Bros. & Co.*, 240 U.S. 251, 258 (1916); *American Construction Co.* v. *Jacksonville, T. & K. W. Ry.*, 148 U.S. 372, 384 (1893); *cf. Youngstown Sheet & Tube Co.* v. *Sawyer*, 343 U.S. 579, 584-85 (1952). Indeed, the Court has held that the lack of finality of a judgment of the Court of Appeals alone justifies the denial of certiorari. For example, in *Brotherhood of Locomotive Firemen* v. *Bangor & Aroostook R.R.*, 389 U.S. 327, 328 (1967) the Court said that "because the Court of Appeals remanded the case, it is not yet ripe for review by this Court." Thus, denying the Milsteins' petition for certiorari at this time clearly does not preclude them from seeking to obtain review by this Court on the 13(d) question on a final judgment. *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481, 488, n.6 (1968), *reh. denied*, 393 U.S. 901; *Mercer* v. *Theriot*, 377 U.S. 152, 153-54 (1964), *reh. denied*, 377 U.S. 973; *Hamilton-Brown Shoe Co.* v. *Wolf Bros. & Co.*, *supra*. However,

GAF's only opportunity for review by this Court may well be now, as the determination of the Court of Appeals below dismissed GAF's complaint insofar as its 10b-5 claims are concerned. *Toledo Scale Co.* v. *Computing Scale Co.*, 261 U.S. 399, 418 (1923).

Nevertheless, as previously noted, GAF intends to vigorously oppose the Milsteins' application for certiorari. And although the 10b-5 question presented herein is important and worthy of consideration by this Court, GAF prefers to proceed in the District Court without further delay to pursue its remedies under Section 13(d). Should this Court, however, grant the Milsteins' petition, then it should grant this petition. Otherwise further review of the 10b-5 question may be precluded.

5. Barring the issuer from enjoining violations of Rule 10b-5 affecting its own stock frustrates the enforcement of Section 10(b) because the issuer is the most logical and knowledgeable plaintiff and has the resources to prevent the violations.

The case at bar vividly highlights the many reasons which require that the issuer have standing to enjoin violations of Rule 10b-5 affecting its own stock. The issuer is infinitely better positioned than are its shareholders, the Commission, or, for that matter, any other potential plaintiff to protect its shareholders' interests vis-à-vis manipulations respecting its stock. The court below in the context of Section 13(d) noted that "it is fair to assume that [the issuer] scrutinizes carefully changes in its stock ownership" (PP App. A 20a). The issuer can be counted upon to "promptly and effectively police" shareholder filings and it alone has the "day-to-day familiarity with the facts which would enable it to appraise accurately the statements" made in such filing (*Ibid.*). And it is undeniably true that the current knowledge the management has as to the value of the company's assets, its estimated future earnings, likely corporate growth and other relevant economic factors, each

of which bears significantly upon the market price of its securities, enable the issuer to recognize unlawful manipulations in its securities earlier than anyone else. Few, if any, shareholders can approach the level of management's current information respecting these matters and most shareholders lack the facilities and resources to undertake the task. As the court below also noted, "[s]tockholders are generally unaware of the necessary background information to judge the truth or falsity of the statements" (PP App. A 21a). Moreover, absent the prospect of recovering substantial damages little incentive exists for a shareholder to bring suit. These indisputable circumstances, coupled with the fact that the issuer is almost always better able than an individual to afford the expenses of litigation, make it clear that the interests of shareholders and the investing public are best served by permitting the issuer to seek injunctive relief before substantial damage is done to shareholders, prospective investors, and the company itself.

Manipulations of its stock frequently cause extensive and irreparable injury to the corporation. Where the unlawful activities have the effect of depressing the market price the issuer may be severely disadvantaged in negotiations looking to acquisitions and mergers, in marketing its own securities, and in certain types of borrowings. As Chief Judge Friendly of the Court of Appeals for the Second Circuit observed, there are "many practical advantages" supporting standing on the part of the issuer to seek injunctive relief under Rule 10b-5. *General Time Corp.* v. *Talley Indus., Inc.*, 403 F.2d 159, 164 (2d Cir. 1968), *cert. denied*, 393 U.S. 1026 (1969); see Note, Private Enforcement under Rule 10b-5: An Injunction for the Corporate Issuer? 115 U.Pa.L.Rev. 618, 628-29 (1967).

In *J.I. Case Co.* v. *Borak*, 377 U.S. 426, 433 (1964) this Court emphasized the practical difficulties the Commission faces in trying to uncover and prosecute violators of the 1934 Act and stressed the necessity of providing effective private enforcement:

> ". . . [I]t is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose . . . [and] 'to adjust their remedies so as to grant the necessary relief' where federally secured rights are invaded."

In *Borak* the Court created an implied right of action on behalf of a stockholder to challenge the accuracy of a proxy statement disseminated by an issuer because:

> "[p]rivate enforcement of the proxy rules provides a necessary supplement to Commission action. As in the anti-trust treble damage litigation, the possibility of civil damages or injunctive relief serves as a most effective weapon in the enforcement of the proxy requirements."

The Court of Appeals for the Second Circuit followed *Borak* in *Studebaker Corp.* v. *Gittlin*, 360 F.2d 692, 698 (2d Cir. 1966) where the target corporation was granted the same standing as the Commission to enjoin proxy violations. The line of reasoning by which *Borak* and *Gittlin* found that equitable relief to enforce Section 14(a) was proper is equally applicable to Section 10(b). Both sections proscribe unfair and undesirable practices in securities transactions and, if a private party may assist the Commission to police one, it should be permitted to help police the other.

The Court of Appeals for the Second Circuit in *Ruckle* v. *Roto American Corp.*, 339 F.2d 24, 28 (2d Cir. 1964), also recognized the desirability of a corporate right of action in a derivative suit to enjoin the issuance of securities, even

though the damage sought to be prevented would have been to the shareholders:

> "Barring suit by a corporation defrauded under those circumstances would, as a legal and practical matter, destroy any remedy against the perpetrator of the fraud. Suits by individual shareholders would either run afoul of privity requirements or result in smaller recoveries based on loss to individual investments, which would also be difficult to compute." (citation omitted).

And in its decision below, the Court of Appeals emphasized the importance of supplementing Commission action with private enforcement, at least insofar as Section 13(d) is concerned, specifically noting:

> "An already overburdened Commission staff, taxed with reviewing increased filings under the securities acts, should welcome 'a necessary supplement' to its action." (PP App. A 20a)

The tenor of the 1934 Act is prophylactic and its intent is to *prevent* securities frauds. Injunctions are surely an appropriate remedy to maintain fair and honest securities markets and are the only method of *preventing* injury to innocent investors.

The fact that this proceeding arose in connection with a control contest and that the GAF management may not be a "disinterested" party, relied upon by the District Court (PP App. B 20b-21b), should not cloud the importance of the issue presented for this Court's consideration. The Court of Appeals for the Second Circuit, in at least two opinions, has ruled that the standing of a corporation to seek injunctive relief under Section 14 is not precluded by reason of the management's potential or actual self-interest in defending against a takeover attempt. *Electronic Specialty Co.* v.

International Controls Corp., 409 F.2d 937 (2d Cir. 1969); *Studebaker Corp.* v. *Gittlin, supra.*

In matters affecting the securities markets rarely is self-interest not involved. The Court of Appeals in this case specifically acknowledged that the issuer's self-interest was a substantial factor militating in favor of granting it standing to seek injunctive relief under Section 13(d) (PP App. A 17a-18a). As noted above, among all potential plaintiffs, it is the issuer which is ideally situated to recognize 10b-5 violations affecting its own stock and has the resources to prevent and redress those violations. If the violations occur as a prelude to or during a control contest, *nisi prius* courts may be directed to examine management's 10b-5 claims with special scrutiny. But it disserves shareholders and the investing public to completely close the Court House to the presentation of those claims simply because the management has an interest.

The Court of Appeals carefully declined to entirely foreclose the matter of the issuer's standing under 10b-5 (PP App. A 22a-23a). It concluded that since it had found that GAF had standing under Section 13(d), there was "no compelling reason" to grant standing under Rule 10b-5 (PP App. A 22a). We do not quarrel with that conclusion and, as noted earlier, GAF wants to pursue its remedies in the District Court without further delay in accordance with the decision of the Court of Appeals. It is only if this Court should grant the principal petition that we request that, for all of the reasons set forth above, the writ issue to review the issuer's standing to seek injunctive relief under Rule 10b-5.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that in the event the Court should grant the petition for a writ of certiorari in No. 71-1144, this conditional cross-petition for a writ of certiorari should likewise be granted.

Respectfully submitted,

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March 9, 1972.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-1161

GAF CORPORATION,
Conditional Cross-Petitioner,

v.

PAUL MILSTEIN, SEYMOUR MILSTEIN, GLORIA MILSTEIN FLANZER and MORRIS MILSTEIN

STATEMENT OF RESPONDENTS IN RESPONSE TO CONDITIONAL CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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The question of standing under Rule 10b-5, 17 C. F. R. § 240.10b-5, alone, would not justify further review by this Court in this action. On the other hand, in order that the entire case might be before the Court, we have no objection to the "Conditional Cross-Petition" if the principal petition —No. 71-1144—is granted.

Respectfully submitted,

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